

STATE OF IOWA
PROPERTY ASSESSMENT APPEAL BOARD

23rd Street Hotel Associates,
Petitioner-Appellant.

v.

Pottawattamie County Board of Review,
Respondent-Appellee.

ORDER

Docket No. 10-78-0272
Parcel No. 7444 03 400 014

On February 14, 2012, the above-captioned appeal came on for hearing before the Iowa Property Assessment Appeal Board. The appeal was conducted under Iowa Code section 441.37A(2)(a-b) and Iowa Administrative Code rules 701-71.21(1) et al. Deborah Tharnish of Davis Brown, Des Moines, Iowa represented the petitioner-appellant 23rd Street Hotel Associates. Assistant County Attorney Leanne A. Gifford represented the Pottawattamie County Board of Review. The Appeal Board now having examined the entire record, heard the testimony, and being fully advised, finds:

Findings of Fact

23rd Street Hotel Associates (23rd Street), owner of property located at 2702 Mid America Drive, Council Bluffs, Iowa, appeals from the Pottawattamie County Board of Review decision reassessing its property. The real estate was classified commercial for the January 1, 2010, assessment, and valued at \$14,000,000; representing \$385,000 in land value and \$13,615,000 in improvement value. 23rd Street protested to the Board of Review on the ground the property's assessment was not equitable with the assessments of other like property under Iowa Code section 441.37(1)(a); and the property was assessed for more than authorized by law under section 441.37(1)(b). The Board of Review denied the protest.

23rd Street then appealed to this Board asserting the same grounds. On its appeal form, 23rd Street asserted the correct assessment is \$9,119,205; allocated \$385,000 to land and \$8,734,205 to improvement. It now seeks an assessed value of \$8,420,000 based on an appraisal of the subject property, which excludes the land lease payments and furniture, fixtures, and equipment (FF&E).

The subject property, locally known as the Hilton Garden Inn, is adjacent and connected to the Horseshoe Casino. The land the improvements and additional parking are located on is leased from HBR Realty Company, which is also the owner of the adjacent casino. The lease has a term of forty-eight years. We question why the land is assessed to 23rd Street. However, neither party raised that issue on appeal. Therefore, we will not address that issue. The land area covers the area under the hotel and an additional 38,768 square foot parcel consisting of 400 parking spaces, which are 105 square feet each.

The subject property is a five-story, steel-frame building with EIFS exterior. Common areas include a reception area, lobby, restaurant with bar, office area, meeting rooms, and a pool. It was built in 2009 and has 153 rooms, including 32 suites.

Bruce Kinseth, owner/operator of 23rd Street testified at hearing regarding the property's assessment. Kinseth has been in the hotel/hospitality business for approximately thirty years. His corporation currently has an interest in about thirty-five properties, while managing about 105 properties located mostly in the upper Midwest. He testified regarding the economic condition of the hotel industry in the last few years. Kinseth stated when they made the decision to build next to the casino, he had an agreement with Harrah's Casino to rent up to half the rooms out at about \$90 per room. Kinseth stated they started the construction prior to the recession, noting at the time the area market was strong, and in all likelihood would not have gone ahead with the project if he had anticipated a market decline. Generally, occupancies fell dramatically in 2009, and then rents started

to fall. The hotel's rents have dropped off since it opened in October 2009. He stated he believed the hotel opened at "the worst possible time."

Kinseth testified regarding 23rd Street's performance at the end of 2009, following its opening as well as its performance in 2010 and 2011. 23rd Street introduced exhibits 7, 8A-8C, 11, 12, and 13, which mostly related to this testimony and reflected dates ranging from 2009 through 2011. The Board of Review objected to these documents based on relevance, arguing the dates reflected in the documents post-date the assessment date. The documents were admitted subject to the objection. The information contained in these reports shows the subject property's performance as it relates to competing properties, and much of the information does post-date the assessment. 23rd Street believed the information was relevant because the property had only been operating for three months at the time of the assessment date. Kinseth testified he believed the information shows a market "free-fall" and the recession truly accelerating. He also testified they were still in the "ramp-up" stage on January 1, and the stage ended in about July 2010. While the information may help demonstrate Kinseth's beliefs about the market, this evidence is not the best evidence in the record to show the subject property is inequitably or over-assessed, and we give it little weight.

Kinseth also believes 23rd Street should be assessed equal to Springhill Suites and the Holiday Inn Express and Suites since they are all competitive, top-quality hotel brands, with similar locations and new facilities. Kinseth notes that Springhill, which has all suites and are, on average, 100-square feet larger than the subject, is assessed at \$59,602 and the Holiday Inn Express, which has about 20% suites similar to the subject, is assessed at \$57,500. The Springhill and Holiday Inn both were assessed by using both the cost and income approaches to value the properties. 23rd Street, however, is assessed at about \$91,503 per room, and its assessment is based solely on cost.

23rd Street called Pottawattamie County Assessor Bill Kealy, over the objection of the Board of Review. Kealy testified that he did not do a sales approach to value on 23rd Street, Springhill, or

the Holiday Inn Express. Kealy stated he used the *Iowa Real Property Appraisal Manual* to value the properties. However, he also used the income approach, in addition to the cost approach, on Springhill and the Holiday Inn Express. He stated he did not use the income approach for 23rd Street because income information was not provided. Kealy testified his office essentially did an estimated value on the subject property because the office did not have cost and income information from Kinseth. Kinseth stated he did not return to the assessor the request for construction cost or income data, since 1) it was a start-up and income was not reflective of market at the time and 2) the construction cost was not relevant to the return on investment at the time of construction. In his opinion, the valuation should be on "like kind" property, meaning new hotels such as Springhill and the Holiday Inn.

Kealy stated that he does not gather income expense data every year or every two years; he only gathers construction costs and income data when the properties are newly constructed. He noted the office also considers permit costs as part of the information available to it. At its hearing before the Board of Review, Kinseth did provide 23rd Street income data, which the Board could have used.

Ted Frandson of Frandson & Associates, LC, Des Moines, Iowa, completed an appraisal of the subject property as of January 1, 2010, on behalf of 23rd Street. He also testified on its behalf at hearing. Frandson's estimate for the real estate only was \$8,420,000. Frandson used all three approaches to value.

Frandson stated he gave less weight to the cost approach, even though typically this approach is a good indication of value when the property is new. His reason for giving it less weight was due to the current condition of the hotel market, and in his opinion, the property's external obsolescence. Frandson determined a land value using three comparable sales in Council Bluffs. After adjustments, he determined a square-foot value of \$14.00 for the subject site was appropriate, for a total value of \$540,000 (rounded). He then determined the cost of the improvements less depreciation and furniture, fixtures, and equipment. He used *Marshall and Swift Valuation Service* and also considered cost as

reported by the developer. He determined a total value for the real property using the cost approach of \$11,831,000.

In his sales comparison approach, Frandson used three sales in the Omaha, Nebraska, area. He admitted during this time frame very few comparables existed because of the recession and ultimately chose three sales from 2008 as comparables. However, he believed this approach was a reliable indication of value. The sales all occurred in 2008 and were of properties with “comparable construction and finish quality to the typical higher range full service or limited service hotel.” Frandson indicated that the market area and location were of the greatest importance and then he focused on similar “flags” or hotel brands. He made adjustments for market conditions, location, room count, gross area per room, quality/finish, and site improvements. Frandson was cross-examined regarding the use of a 1031 exchange sale located at 3404 Samson Way. He explained he believed that despite the 1031 exchange, the transaction was arm’s-length or if anything it would have made the sales price slightly higher. The adjusted values provided an indicated value per room of \$61,958 to \$72,250. He used a per-unit value of \$65,000 to arrive at a total sales approach value of \$9,945,000 (including FF&E).

In the income approach he considered that since this was a start-up hotel operation and would take time to stabilize, the actual income was considered to be reflective of market rents. To arrive at this conclusion, Frandson did consider the market rates of seven other properties in the subject’s area. He arrived at a net operating income (NOI) of \$1,181,007 and used an adjusted overall capitalization rate of 12.99% to arrive at an indicated value using the income approach of \$9,092,000 (rounded).

Frandson arrived at a final reconciled value of \$9,500,000 (including FF&E), giving most weight to the sales and income approaches and very little weight to the cost approach. He then subtracted out \$1,080,000 for non-taxable property, and concluded a total value of the subject property at \$8,420,000.

At the end of 23rd Street's presentation of evidence, the Board of Review moved for a directed verdict. The Board of Review argued 23rd Street failed to prove the property was inequitably assessed or over-assessed because of the perceived flaws it found in the Frandson appraisal. This Board denied the motion. The evidence in the record was enough to proceed. Assessor Kealy testified he used different methods to assess other like hotels and in this Board's opinion Frandson's appraisal was competent evidence to the January-1, 2010, market value.

Gary DeClark of Integra Realty Resources, Chicago, Illinois, testified at hearing regarding the appraisal he completed of the subject property as of January 1, 2010, for the Board of Review. Like Frandson, DeClark estimated values using all three approaches to value.

DeClark considered the cost approach to be a good indication of value since the property is new and, in his opinion, investors would look at the cost to develop similar type assets. DeClark made no adjustment for external obsolescence in his cost approach. He determined a value from the cost approach of \$16,915,000 (rounded).

DeClark gave primary weight to his sales comparison approach. He used five sales: three in Texas, one in Arizona, and one in Colorado. None of the sales are located in the same market area as the subject property, and in fact, are not even located in the Midwest. DeClark claimed this was because the "flag" on the property was more important for comparison sake than the market area. As previously noted, Frandson indicated it was his belief that market area was of more importance. We agree with Frandson. The geographic distance of the properties and primarily the fact that they are not located in the same market area as the subject property make them less comparable than the properties chosen by Frandson in his appraisal. DeClark's sales comparison approach resulted in a value of \$16,065,000.

DeClark gave very little weight to his income approach. Since the subject property is new, in his opinion, the property is not fully entrenched in the market. His income approach value was \$12,935,000.

DeClark's final estimate of value was \$16,000,000 for the real estate only.

In his appraisal, DeClark did not make percentage adjustments. Instead, he indicates differences between his comparable properties with arrows pointing up or down. His reason was that people tend to focus on the adjustments and a lot of the adjustments are based purely on judgment. He also indicated he would have no way to support an exact percentage adjustment (for example a 20% upward adjustment). DeClark did, however, testify at hearing regarding the percentage adjustments the arrows were intended to represent and at the end of the hearing the Board of Review, submitted a one-page exhibit (D) that had percentage adjustments for only his sales approach. He did not have adjustments for land sales. This exhibit should have been produced before the hearing started so the appellant could question DeClark; it should have also been included in the appraisal itself to provide explanation for the reader. He continued to testify about the adjustments of the economy being up and down. DeClark also testified to how property is assessed in Iowa for property tax purposes. When questioned by this Board regarding his intangible reference in the appraisal and adjustments, it became clear that this was the first time he testified regarding property tax in Iowa. We also find DeClark's appraisal, without the additional sales adjustment exhibit, made it nearly impossible for this Board to consider the comparability of the sales he chose and determine their reliability. Additionally, as previously noted, DeClark used sales outside the market area, and he was not clear on how he accounted for location difference, which is a basic "appraisal 101" type of consideration. We did not find DeClark to be credible regarding the determination of the assessed value of the subject property as of January 1, 2010.

We find Kinseth was very knowledgeable regarding the hotel/hospitality industry and honest regarding his current rents and the impact of the hotel recession. The current economy had an impact on his agreement with the casino room rates, and the competition from other hotels has diminished 23rd Street's current income.

Finally, we find Frandson's appraisal to be the best evidence in the record. He testified that comparables are difficult to find because of the poor hotel market in 2010. His actual income reflected the market rent for a start-up hotel, and unlike DeClark, he did not disregard the income approach to value. We find Frandson to be the more knowledgeable and the credible appraiser of the two regarding the determination of the value of the subject property.

It was also clear that Pottawattamie County valued Springhill and Holiday Inn Express differently than they valued Hilton Garden. Springhill and Holiday Inn are valued at \$59,600 and \$57,500 per room and Hilton at \$91,500. Finding the property was perhaps inequitably assessed since different methods were used to assess it as compared to similar properties and that it was, in fact, over-assessed based on Frandson's appraisal, we modify the assessment determined by the Board of Review, to \$8,420,000 as of January 1, 2010.

Conclusions of Law

The Appeal Board based its decision on the following law.

The Appeal Board has jurisdiction of this matter under Iowa Code sections 421.1A and 441.37A (2011). This Board is an agency and the provisions of the Administrative Procedure Act apply to it. Iowa Code § 17A.2(1). This appeal is a contested case. § 441.37A(1)(b). The Appeal Board determines anew all questions arising before the Board of Review related to the liability of the property to assessment or the assessed amount. § 441.37A(3)(a). The Appeal Board considers only those grounds presented to or considered by the Board of Review. § 441.37A(1)(b). But new or additional evidence may be introduced. *Id.* The Appeal Board considers the record as a whole and all

of the evidence regardless of who introduced it. § 441.37A(3)(a); *see also Hy-vee, Inc. v. Employment Appeal Bd.*, 710 N.W.2d 1, 3 (Iowa 2005). There is no presumption that the assessed value is correct. § 441.37A(3)(a).

In Iowa, property is to be valued at its actual value. § 441.21(1)(a). Actual value is the property's fair and reasonable market value. *Id.* "Market value" essentially is defined as the value established in an arm's-length sale of the property. § 441.21(1)(b). Sales prices of the property or comparable properties in normal transactions are to be considered in arriving at market value. *Id.* If sales are not available, "other factors" may be considered in arriving at market value. § 441.21(2). The assessed value of the property "shall be one hundred percent of its actual value." § 441.21(1)(a).

To prove equity, a taxpayer may show that an assessor did not apply an assessing method uniformly to similarly situated or comparable properties. *Eagle Food Centers v. Bd. of Review of the City of Davenport*, 497 N.W.2d 860, 865 (Iowa 1993). Alternatively, a taxpayer may show the property is assessed higher proportionately than other like property using criteria set forth in *Maxwell v. Shriver*, 257 Iowa 575, 133 N.W.2d 709 (1965). The six criteria include evidence showing

"(1) that there are several other properties within a reasonable area similar and comparable... (2) the amount of the assessments on those properties, (3) the actual value of the comparable properties, (4) the actual value of the [subject] property, (5) the assessment complained of, and (6) that by a comparison [the] property is assessed at a higher proportion of its actual value than the ratio existing between the assessed and the actual valuations of the similar and comparable properties, thus creating discrimination."

Id. at 579-580. The gist of this text is the ratio difference between assessment and market value, even though Iowa law now requires assessments to be 100% of market value. § 441.21(1). Based on Assessor Kealy's testimony, we find the subject property was assessed differently than other similar hotels, which under *Eagle Foods* is impermissible.

In an appeal that alleges the property is assessed for more than the value authorized by law under Iowa Code section 441.37(1)(b), there must be evidence that the assessment is excessive and the

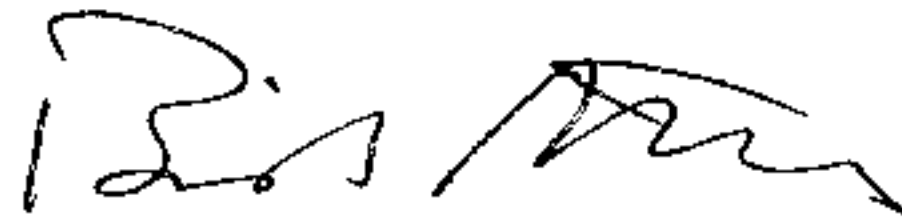
correct value of the property. *Boekeloo v. Bd. of Review of the City of Clinton*, 529 N.W.2d 275, 277 (Iowa 1995). There is statutory preference for establishing market values using sales of comparable properties. *Soifer v. Floyd County Board of Review*, 759 N.W.2d 775, 779 (Iowa 2009). The issue of comparability has two facets: the property must be comparable and the sale of that property must be a “normal transaction”. *Id.* at 782-83. When sales of other properties are offered, they must be adjusted for differences that affect market value. *Id.* at 783. These differences could include size, age, use, condition and location, among others. *Id.* The Court of Appeals has held “mental adjustments” to comparable sales that are not translated into specific dollar amounts or a percentage adjustment limits the fact finder’s ability to make a determination as to whether the sales comparison approach is reliable. *Dowden v. Dickinson County Bd. of Review*, 338 N.W.2d 719, 723 (Iowa Ct. App. 1983). The Iowa Supreme Court has also recently noted that an appraisers failure to quantify adjustments “makes an informed evaluation of the credibility of a comparable-sales valuation difficult,” and had the opinion “been offered to support an actual value equal to [the appraisers] valuation, [the Court] would be more concerned about the precision of adjustments.” *Soifer*, 759 N.W.2d at 789. DeClark’s appraisal did not explain or quantify his adjustments. Only at hearing, did he describe adjustments to the sales comparables and offer an adjustment chart. Even though he ultimately described the adjustments, we find his comparable sales are not as reliable based on their location. Frandson’s appraisal is the best evidence in the record and shows the property is over-assessed and its market value as of January 1, 2010 assessment should be.

The evidence in the record supports the claims of over-assessment brought before this Board. We, therefore, modify the assessment of the subject property located at 2720 Mid America Drive, Council Bluffs, Iowa, as determined by the Pottawattamic County Board of Review as of January 1, 2010.

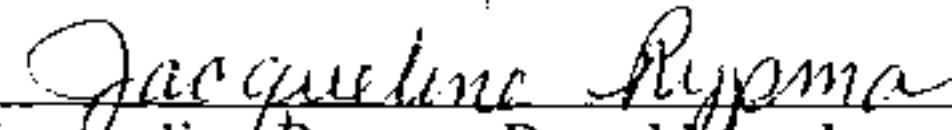
THE APPEAL BOARD ORDERS that the January 1, 2010, assessment as determined by the Pottawattamie County Board of Review is modified to \$8,420,000.

The Secretary of the State of Iowa Property Assessment Appeal Board shall mail a copy of this Order to the Pottawattamie County Auditor and all tax records, assessment books and other records pertaining to the assessments referenced herein on the subject parcels shall be corrected accordingly.

Dated this 19 day of April 2012.



Richard Stradley, Presiding Officer



Jacqueline Rypma, Board Member



Karen Oberman, Board Member

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Certificate of Service	
The undersigned certifies that the foregoing instrument was served upon all parties to the above cause & to each of the attorney(s) of record herein at their respective addresses disclosed on the pleadings on <u>4-19</u> , 2012.	
By:	<input checked="" type="checkbox"/> U.S. Mail <input type="checkbox"/> FAX
	<input type="checkbox"/> Hand Delivered <input type="checkbox"/> Overnight Courier
Signature	